



April 5, 2004

Docket No. 04-06
Communications Division
Public Information Room, Mailstop 1-5
Office of the Comptroller of the Currency
250 E St. SW,
Washington 20219

Docket No. R-1181
Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington DC 20551

Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th St NW
Washington DC 20429

Regulation Comments, Attention: No. 2004-04
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street NW
Washington DC 20552

Dear Officials of Federal Bank and Thrift Agencies:

The ShoreBank Corporation ("ShoreBank") appreciates the opportunity to comment on the proposed changes to the Community Reinvestment Act (CRA or Act) regulations

published in the Federal Register on February 6, 2004. ShoreBank urges you to withdraw the proposed changes to the Community Reinvestment Act (CRA) regulations. CRA has been instrumental in increasing access to homeownership, boosting economic development, and expanding small businesses in the nation's minority, immigrant, and low- and moderate-income Communities. We feel that the proposed changes to the CRA regulation will significantly roll back policy essential for community reinvestment and misses a critical opportunity to close loopholes and modernize the CRA regulation.

ShoreBank has long been a proponent of enhancing CRA regulations and has seen the effect this regulation has on the communities we serve. As the country's first, and largest, community development financial institution, ShoreBank has garnered critical deposits from numerous large and small banking institutions as a result of CRA. These deposits have enabled ShoreBank to deliver over \$1.5 billion dollars in loans and investments to disadvantaged communities throughout the United States. ShoreBank's investments, in turn, have resulted in the rehabilitation of tens of thousands of affordable housing units and the growth of thousands of small businesses. Changes to CRA could greatly diminish our ability to continue this work.

Specific concerns include:

Small Bank Limits

The proposed CRA regulation would change the definition of "small bank" from any institution with less than \$250 million in assets and not part of a holding company with over \$1 billion in assets to include all institutions with less than \$500 million in assets regardless of holding company size. This change will dramatically increase the number of banks considered "small" that, for CRA purposes, are not examined for their levels of community investment and services under the streamlined small bank CRA examination. We are opposed to this change, despite the fact that this new rule would exempt two of our subsidiary banks from the "large" bank examination guidelines to which they are now subject. However, because of the disproportionate affect this change will have on rural communities and small cities where smaller institutions have significant market share, we are obliged to oppose the change. Indeed, according to the Woodstock Institute, in Illinois it will reduce the number of institutions covered by the comprehensive CRA exam by 63 percent, from 198 banks to 74. However in rural areas or small cities, the number of institutions covered by comprehensive CRA will decline by nearly 73 percent. In these communities, already struggling, banks will be less compelled to provide innovative investment opportunities and services. Additionally, these banks will no longer be required to report small business lending data. This will significantly reduce available data on small business lending despite the fact that it has

been shown that small banks have a larger share of their lending dedicated to small businesses than larger banks.

Affiliate Lending and Assessment Areas

Regulators missed a significant opportunity to modernize CRA by not requiring affiliate lending to be considered in CRA exams. As bank holding companies increasingly use non-bank lenders to originate mortgages, it is critical that all lending affiliates be required to report lending in an institution's CRA exam. As currently structured, the CRA regulation allows banks to choose which affiliate loans in a given assessment area they want to apply toward the lending test. This loophole allows institutions to cherry pick the best lending affiliates for each assessment area and exclude affiliates in assessment areas where those affiliates might not be adequately serving the community. As holding companies increasingly acquire non-bank lenders, including predatory lenders, it is critical that this loophole be closed and all lending affiliates be considered in CRA exams.

Additionally, we were disappointed to see that there was no change to how assessment areas are considered. As technology and regulatory policy has advanced to allow financial institutions to conduct business through channels other than traditional branches, CRA has not advanced with it. To have this level of lending not fully considered in an institution's CRA exam gives banks another loophole to exploit in evading full CRA compliance.

The Investment Test

For many of the reasons stated in the preamble to the NPR, ShoreBank is a strong supporter of the investment test. We believe that community development investments, including grants and equity investments that enable community development organizations to grow in both size and effectiveness, are critically important to the health of our communities especially those that have been traditionally underserved by many entities subject to CRA. Nevertheless, as a holding company for banks (including two very small banks) that are, or under current regulations will be, subject to the large-bank CRA examination, we are cognizant of some of the ambiguities and pitfalls in the current investment test, including the possibility of different interpretations by different agencies and even different examination teams.

Thus, we are disappointed the agencies did not tackle some of these problems in the NPR, and have rather left them to the interagency guidance process. The NPR is

already over two years in the making, and the agencies have had the benefit of 400 comment letters, many of them focused on the investment test. In particular, we strongly urge the regulators to revise the regulations to include, in regulatory text, the items relating to the investment test discussed in the preamble, in particular (i) the impact of activities outside a bank's assessment area; (ii) that effectiveness is at least as important in evaluation as whether an investment is "innovative" or "complex"; (iii) the manner in which outstanding equity-like investments in community development organizations will be given credit in years other than the initial investment year; and (iv) the manner in which an investment's "primary purpose" will be determined. These issues should be dealt with in the context of regulatory text, not guidance, and the time for public comment on such text is now.

Predatory Lending Standard

By mirroring the OCC and setting a weak anti-predatory lending standard, regulators missed a significant opportunity to make a strong statement about predatory lending. The proposed standard allows that loans originated based on foreclosure value of collateral rather than borrower ability to repay can negatively affect a bank's CRA exam. This standard misses numerous predatory practices such as packing exorbitant fees onto mortgage loans, loan flipping, charging high prepayment penalties, and mandatory arbitration that can strip equity from homeowners and trap borrowers in abusive loans. Regulators should apply a strong predatory lending standard to bank loans and to loans made by affiliates.

Data Disclosure

We welcome additional data disclosures on CRA exams, but feel the data need to be more fully considered in evaluations to be truly effective. Reporting the census tract location of an institution's small business loans will allow for greater understanding of how banks serve traditionally underserved communities. However, the benefit of this additional data is partly offset by loss of data for banks that would be considered "small" under new criteria. These lenders are significant providers of small business loans, and the loss of this data will create a significant gap in available data. Additionally, adding data to CRA exams to differentiate between the share of bank and affiliate loans that are originated and purchased and those which are high interest rate and HOEPA loans is also a positive step, but these loans should not be weighted equally. Originated, lower interest rate, and non-HOEPA loans should be given more weight.

ShoreBank welcomes the additional data disclosures, but feels that proposed changes undermine the mission of community reinvestment by creating loopholes for financial institutions to exploit and evade significant CRA compliance. We also feel regulators missed a significant opportunity to modernize CRA to reflect the reality of how financial services are provided today. We urge you to reject the proposed changes to the definition of small banks; adopt a more inclusive policy toward affiliate lending and assessment areas; strengthen the proposed predatory lending standard; and maintain the data disclosure proposal.

Sincerely,

Ronald Grzywinski
Chairman, ShoreBank Corporation

Anne Arvia
President & CEO, ShoreBank